Transitional Stability Plan Option

I. Establish an Interim Universal Broadband Service Requirement

Adopt the proposed 4 Mbps down / 1 Mbps up broadband speeds as an interim universal service standard subject to annual review and adjustment to maintain reasonably comparable rates and services in rural areas with those available in urban areas.

II. Provide Revenue Assurance/Stability for recovery of established investment and operating expenses by providing rate-of-return carriers with the option to freeze their existing interstate revenue requirement, subject to upward and downward adjustments consistent with the Commission's universal service objectives.

A. Freeze each electing rural ROR carrier's interstate revenue requirement (including high cost loop fund support) as of a date certain (e.g., December 31, 2012), subject to adjustments to reflect additional committed capital and increased expenses resulting from RUS or Broadband stimulus project commitments, and adjustments needed to provide an expanded definition of universal service.

As a result of the initial interstate revenue requirement freeze, the electing carrier's existing aggregate USF funding and interstate access revenue requirement (including ICLS) will be constrained and reduced each year, as discussed below. In the event that the electing carrier subsequently incurs additional capital or operational expenses needed to provide universal service and, as a result, requires additional universal service support, any such support will be derived from the Commission's new Connect America Fund (CAF); and any such additional expenses shall be identified separately within the appropriate Part 32 account.

Each company currently subject to rate-of-return regulation may make an election to utilize this methodology to determine its future interstate revenue requirement by submitting notice of its election to the Commission by July 1, 2012.

1. Determination of first annual period interstate revenue requirement for an electing carrier.

(a) For the first annual period during which this election is effective for a cost company, the electing company's total interstate revenue requirement will be based on the electing company's most recent cost of service study adjusted consistent with item (c) below.

(b) For an electing company that is an average schedule carrier, the electing company's total interstate revenue requirement will be the sum of that company's prior year settlement from the National Exchange Carrier Association ("NECA") pool, prior year subscriber line charges, and prior year USF revenues, adjusted consistent with item (c) below.

(c) The electing company's initial interstate revenue requirement, as established by section (a) or (b) above shall be adjusted to reflect any additional depreciation expense and adjustment to the return on investment necessary to reflect additions to capital investment arising from capital commitments incurred by the electing company prior to December 31, 2011 as a result of participation in Rural Utility Service ("RUS") financing or RUS or NTIA broadband stimulus programs, or other capital commitments made prior to December 31, 2011. With regard to any such capital commitments, revenue requirements shall be adjusted in accordance with Part 32 and Part 36 regulations as additional plant is placed into service.

2. Determination of subsequent annual period adjustments to the interstate revenue requirement of an electing carrier.

The subsequent period interstate revenue requirement for each electing company will be reduced in accordance with the carrier's election to utilize option (a) or (b) below. The electing company shall make a one-time determination of which option it will utilize and notify the Commission of its election concurrent with the provision of the company's notice to the Commission required by Section A, above.

(a) The electing company's interstate revenue requirement shall be reduced annually by that amount equal needed to reflect the reduction in the company's total regulated plant in service less accumulated depreciation as determined annually in accordance with Part 32 of the Commission's rules for purposes of conducting a cost of service study pursuant to Part 36 of the Commission's rules.

(b) Alternatively, the electing carrier may elect that its interstate revenue requirement shall be reduced annually by the total of 3% reduced by one-half of the nationwide CPI inflation factor.

B. ***Maintaining a Rate of Return Safety Valve Process***

Carriers committed to the provision of universal service must have reasonable assurance of a meaningful opportunity to recover the costs of providing universal service through the continued application of RoR where necessary.

In the event an electing carrier requires additional funding in order to support the provision of an expanded definition of universal service or to maintain the provision of universal service, any funding provided in accordance with the rules proposed below will be derived from the CAF with the following exception.

The electing company may make a one-time only election to return to full rate-of-return regulation and determine its interstate revenue requirement in accordance with the effective jurisdictional separations rules in effect for the determination of the interstate revenue requirement for the subsequent periods in effect at the time of the election, including the utilization of any model adopted by the Commission for the purpose of identifying permissible expense levels to provide universal service in the carrier's study area.

Support requirements from the CAF for an electing carrier will be established in accordance with the following procedures.

1. An electing company seeking CAF support will file cost support to justify the requested increase by July 1 of the year prior to the period for which the company seeks the adjustment. The cost support information will be submitted in a format consistent with FCC Rules Parts 32 and 36; additional proposed capital investment to provide broadband connectivity in accordance with the Commission's (evolving) definition of universal service will be directly assigned to the interstate jurisdiction consistent with the Commission's determination that the provision of broadband transmission service is jurisdictionally deemed interstate. Similar to tariff filing rules, the carrier will provide a description and justification together with the cost support information to demonstrate that the additional investment and expenses proposed for inclusion in the interstate revenue requirement will be used and useful. Any resulting increase in funding will be provided through the CAF.

(a) In order to avoid uncertainty and instability, the FCC will process any request for adjustment to the interstate revenue requirement within no more than 5 months of the date of application, consistent with the underlying policy set forth in Sec. 204 of the Act.

(b) Approved operational expense increases will be added to the company's annual interstate revenue requirement beginning with the following annual period subsequent to the approval. Any such operating expenses shall be separately identified within the company's Part 32 accounting records as "additional CAF funded interstate expenses" and any such expenses will not be subject to the reductions provided by section A.2.(b), above.

(c) Approved capital expense increases (the annual depreciation expense and authorized return on the proposed additional investment) will be added to the company's annual interstate revenue requirement beginning with the following annual period subsequent to the approval. Any such capital expenses shall be separately identified within the company's Part 32 accounting records as "additional CAF funded interstate expenses" and maintained separately within the Part 32 account categories associated with plant and depreciation.

(d) Funding associated with approved adjustments increasing the company's interstate revenue requirement will be distributed from the Commission's Connect America Fund ("CAF"). Depending on how the Commission elects to establish its rule for funding from the CAF, the funding of needed capital investment could alternatively be achieved through one-time funding of requests for capital investment funding.

C. Interstate Revenue Sources

1. Frozen interstate revenue requirement is recovered from Subscriber Line Charges (SLCs), interstate access charge revenues (NECA pooled settlements or individual company billed and kept access revenues) and USF.

2. For electing RoR companies, all elements of High Cost USF support are combined. Recognizing that the High Cost Loop fund is capped, that portion of the capped fund associated with the funding of the electing carriers in 2011 will be established and frozen; the remaining High Cost Loop Funding will continue to be available to the rate-of-return carriers that do not elect the incentive Transitional Stability Plan.

The total USF payment to an electing carrier is derivatively derived:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

Similar to current pooling practices, companies will receive a monthly USF payment from USAC based on projections.

The USF distribution will also include funding from any prospective restructure mechanism established by the FCC to offset revenue losses resulting from reductions in intrastate and interstate access rates contemplated by the FCC.

The access revenue component for an electing company may be obtained either on an individual company basis or a pooled basis within the NECA pools (see, Sec. III, below).

An annual true-up process within USAC will be needed to address long-falls or shortfalls.

III. Intercarrier Compensation – Access Charge Transition

The Transitional Stability Plan proposes two options for rural rate-of-return carriers:

A. Maintain Current Switched Access Charges and Follow The Transition Ultimately Established By The FCC For Rural RoR Carriers.

(1) <u>Pooling</u> – for those electing cost companies that are in the NECA tariff and pools, they will continue to follow the same process that they follow today with the following exception. Instead of providing NECA with an annual cost of service study, the electing company will provide NECA annually with revisions of the results of the cost study utilized to establish the company's initial frozen interstate revenue requirement (see, Sec. II A. 1.); the revisions will reflect the authorized adjustments made consistent with the procedures set forth in Section II, A. 2a. The

frozen annual cost of service study, subject to reductions provided in Section II A. 2, will become the basis for determining the electing company's interstate access revenue requirement in the same way that the annual cost of service study submitted by each cost company is utilized today. The electing company's pooled access settlement revenue is utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

The treatment of average schedule companies electing to participate in the transitional incentive plan option should not require any adjustment within the pooling process. The average schedule company's total annual average schedule settlements are utilized as the "interstate access revenues" in the formula set forth above. With respect to the adoption of a prospective intrastate access charge transition by the Commission, the "Total Interstate Revenue Requirement" will include the amount of intrastate revenue reduction created by reducing intrastate access rates which will be recovered from the RM.

(2) Electing companies that are not in the NECA Pool – any such company may elect to continue to follow the same process that they follow today with the following exception. Instead of revising its annual tariff filing on the basis of an annual cost of service study, the electing company will determine and justify its annual rate filing on the basis of the cost study utilized to establish the company's initial frozen interstate revenue requirement (see, Sec. II A. 1.) with revisions made annually to reflect the authorized adjustments made consistent with the procedures set forth in Section II, A.2.

The revised annual cost of service study will become the basis for the electing company's interstate access filing pursuant to the same process by which the annual cost of service study submitted by each cost company is utilized today. The electing company's resulting interstate access revenue requirement will then be utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

With respect to the intrastate access charge transition, "Total Interstate Revenue Requirement" will include the amount of intrastate revenue loss resulting from intrastate access charge reductions that is shifted to the interstate jurisdiction for recovery from the RM.

B. Access Charge Incentive Option

A rate-of-return carrier may alternatively make an election to utilize price-caps in a manner similar to the option provided to mid-size carriers, utilizing the same rates as the mid-size carriers utilize. The rates will ultimately transition further in accordance with a transition established by the FCC that recognizes the need for revenue recovery from the CAF established RM to replace the lost access revenues.

This option for small rural rate-of-return study areas is distinct from the option provided to the mid-size carriers. Under the mid-size carrier price cap plan, the ICLS element was frozen on a per line basis, and ICLS recovery would diminish as lines are lost, regardless of the fact that there was no reduction in the cost to the carrier to provide carrier of last resort ("COLR") service throughout its study area.

Under this option in the Transitional Stability Plan, the ICLS (or equivalent funding) is not reduced because the total interstate revenue requirement has been frozen (subject to the adjustments provided in Sec. II A.). Operationally, the result is the same as lowering the access charge and recovering the resulting lost access revenues from the CAF RM. The electing company's total interstate access revenues will be utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

To the extent that the FCC subsequently directs a further transition of the (interstate) access charge rates, the resulting access revenue loss will be recovered from additional CAF RM payments.

With respect to any intrastate access charge transition authorized by the Commission, "Total Interstate Revenue Requirement" will include the amount of intrastate revenue requirement shifted to the interstate jurisdiction by the Commission; the resulting additional interstate revenue requirement will be recovered from the RM.

3. Additional Special Access Option

A carrier electing the Transitional Stability Plan incentive proposal should have the additional option to remove its special access costs from its interstate revenue requirement prior to the implementation of the interstate revenue requirement freeze provided for in Sec. II A. Under this option, the carrier would agree to cap its special access rates.

As a result, the carrier would have the incentive to market its special access at or below the capped rates because the revenues would be subject to bill and keep; and these revenues would not offset the interstate frozen revenue requirement (which would have already been reduced to reflect the removal of special access costs).